

Remarks of the Honorable Kathleen B. Cooper  
Under Secretary for Economic Affairs  
The Department of Commerce  
Wednesday, December 5, 2001

Arizona State University  
Economic Forecast Luncheon

As prepared for delivery

I'd like to thank Arizona State University for inviting me to join you today, and Bank One for being a good friend to the university and the community here.

Art Blakemore's economics department teaches more than 12,000 students a year – many aspiring economists, including the Bank One Scholars we recognize today. Given the law of supply and demand, I hope for their sakes that some of those 12,000 aspire to another profession. But thank you Art for giving all your students a lasting interest in economics.

The 38<sup>th</sup> annual Economic Forecast Luncheon has become a fancy Econ 516 class. For those of you who haven't been worrying about registering for upper level classes here at ASU for a while, let me refresh your memory. Econ 516, "Economics of Uncertainty, Information, and Strategic Behavior. The class focuses on economic behavior under uncertainty; markets and contracts under asymmetric information; the theory of games with incomplete information and applications. Prerequisite: ECN 512 or instructor approval." The American economy since September 11 is Econ 516.

Lesson one – Uncertainty. On September 11, I was packing boxes and culling through ten years of family treasures and household junk in Dallas. Just a few months earlier, I'd come to Washington to be the Commerce Department's Under Secretary for Economic Affairs. I thought September would be a good time for the rest of my family and my belongings to make the trip too.

And so I missed the site from my office window that morning. On a clear day I can see the Lincoln Memorial, which is just across the Potomac River from the Pentagon. On that morning, I am told one could see black smoke erupting from the defense headquarters hovering over the 14<sup>th</sup> Street Bridge and Arlington National Cemetery.

The uncertainty on that day and each day that has followed has affected consumers, businesses, and policy makers.

Nonfarm employment fell 415,000 in October – that's the largest monthly decline in 21 years. Questions of when or if the next paycheck will come are bound to cause uncertainty. In the third quarter, 64 percent of employers expected that they would not recall workers from previous layoffs, the highest proportion since the series started in 1995. Of those employers who did expect to recall workers, only half expected to do so this quarter.

So, it was certainly not a surprise last week when the National Bureau of Economic Research reported we are in a recession. But the truth is, before September 11, the confident American consumer buoyed this economy for almost a year. Even as we sensed a slowdown in late 2000 and into 2001, American consumers refused to yield, providing the strong underpinning to the U.S. economy. Despite falling equity market values and rising unemployment, consumers kept buying. Automobile sales and housing sales were resilient. But, business managers reacted with caution. As they began to see future sales in less than glowing terms, they cut back capital spending -- first on a general array of equipment and then on high tech materials.

In the past, business investment and the investment component of household spending have tended to show fairly similar patterns of growth over the course of the business cycle.

In most business cycles, the turns in consumer spending on housing and autos have led business investment. That is, peaks and troughs in household investment spending have taken place before those in business investment. Consumers have tended to be more sensitive to credit conditions than business managers. As a result, households traditionally have responded earlier than businesses to tightening or easing credit conditions near business cycle peaks and troughs. These changing conditions often reflect Federal Reserve policies.

This cycle is different. Business investment weakened much sooner and more significantly than one would expect, given modest credit pressures and the favorable trend so far in household spending. Business investment has been the prime mover in the current downturn. It has contributed most to the decline in total GDP.

We can thank the American consumer for keeping the economy strong for so long. Today's uncertainty about consumer spending and confidence parallel uncertainty about airline safety, anthrax, and the security of bridges. The terrorists must have planned for such a reaction, but they could never have conceived of the incredible national unity their dreadful deeds unleashed. But I am hopeful our countrymen will, in time, pull the economy back to acceptable growth as a "new certainty" emerges.

To emerge, however, we need the information that will allow us to create strategies. Which brings us to lesson two -- Information. One of my surprises in my seven months on the job is just how much information the Economics and Statistics Administration and the Department of Commerce's statistical agencies -- the Census Bureau and the Bureau of Economic Analysis -- produce. I simply had never before tallied their end-product -- GDP, housing starts, retail sales, international trade, construction, inventories, the list goes on. These are major indicators for diagnosing the health and strength of the U.S. economy.

We are committed to improving these data. We are committed to keeping pace with rapid changes in the world around us by using technology to increase accuracy, improve timeliness, and reduce burdens on data suppliers. Moreover, Secretary Evans has taken a

personal interest in our need to better measure the new economy and the services sector. Those are two areas we can do a better job of calibrating and obviously two areas that drive our economy.

The data we release, step by step, form a map guiding policy makers, indeed all Americans, through the uncharted economic world in which we find ourselves after September 11. Here is what we have learned in the past week or so from Commerce Department releases -- all measuring the weeks and the first full month after the attack.

International trade data, released November 20, demonstrated the short-run influence of September 11 and the longer-run effect of global economic weakness. For the first time since 1974, the worlds' three largest economies, the U.S., Germany, and Japan are all declining at the same time. This widespread slowdown has resulted in significant declines in U.S. exports and imports over the last 12 months.

Moreover, the information highlights the need to grant the President Trade Promotion Authority and we expect a vote in the House of Representatives tomorrow. President Bush views trade as a core principle upon which both economic and international policy can be based. Consequently, the Administration has made Trade Promotion Authority a priority. President Bush's ability to negotiate trade pacts will enlarge the sphere in which market economies are allowed to operate for the benefit of people everywhere, but particularly for the benefit of American workers and entrepreneurs.

Single-family houses sold during October released last week demonstrated once again that the housing market is an unusually stable part of the economy owing to the easing of credit throughout the year. The effect of policy -- monetary policy -- shapes and is shaped by such indicators.

While durable goods took a hit in September, October data that we just released shows considerable bounceback. Undeniably, the attacks had a large effect. But we are seeing notable resilience due to several factors: the zero percent financing in the automotive sector, postponed purchases from September, reduced inventories, and the sense that consumers do want to live their lives even understanding the changed circumstances.

These data show decision makers where the economy is weak and where help is needed. How we use this information to confront uncertainty is our strategy and is lesson three.

On September 14 at the National Cathedral the President said, "you will be asked for your patience; for the conflict will not be short. You will be asked for resolve; for the conflict will not be easy."

That day amid the tears, perhaps it seemed that he was speaking only of the conflict with the terrorists. But peace *and* prosperity were attacked. Lives *and* livelihoods were destroyed. I believe he was speaking of our battle for national security *and* economic security. And he has a strategy for both.

National security battles are seen on TV. The economic battles are more subtle, but we feel them. Airport lines at security checkpoints measure a false sense of invulnerability lost. This cost is counted in fewer travelers and the dollars they carry with them. We sensed the echo of an empty hotel filled with shadows of shaken confidence.

In much the same way President Bush has approached the military side of the battle, he developed a strategy and is leading the charge on the home front. He understands these are tough times and more will follow.

The President immediately called for \$40 billion in emergency funding to help the victims, for search and rescue efforts, for the investigation, for airport security and sky marshals, and as a down payment on his commitment to restore the Pentagon and rebuild New York.

The President championed a \$15 billion package for the airline industry, which because of government action was shut down temporarily and sidelined for a week. And before Thanksgiving, President Bush signed airport security legislation.

He has put forward a backstop proposal to make certain that insurance will be available for business activities and operations, so that sensible projects will go forward, airplanes will fly, companies can afford to operate, and the business of America will continue.

All of this spending -- more than \$55 billion -- is not without a positive economic effect. And the President has called for an additional \$60 - \$75 billion in stimulus. He has pledged to extend and expand unemployment benefits to workers displaced as a result of the attack and its repercussions.

But business, the engine of American growth and the driving force in the world economy, needs a jump-start too. A House-passed plan would promote investment and the flow of capital by repealing the alternative minimum tax on business and encouraging investment in new equipment.

An interesting new proposal that came up in the Senate in the past week is a month-long payroll-tax holiday. It would save individuals 6.2 percent and employers the matching amount.

The American people -- consumers, entrepreneurs, workers, and employers -- are on the front lines of the economic battle. The President understands this and wants to know more. Upon his request, Commerce Secretary Evans and the President's economic team have begun to convene a series of economic roundtables across America. The roundtables are comprised of industry leaders, workers, and economists and provide a chance to listen and learn. The first was in Chicago with retailers. Others will be dotted across the country -- highlighting industries from high tech to manufacturing.

The Administration is moving forward with the understanding that declining output in the fourth quarter will likely follow the decline registered in the third. The Administration is moving forward with the understanding that unemployment is on the rise. The

Administration believes both are intolerable and stands ready to employ a strategy to stabilize and strengthen this economy.

Much depends on our citizen soldiers -- their confidence and their job prospects. Many of the factors that made an upturn seem possible on September 10 -- low inflation, low interest rates, declining inventories and energy prices -- are still in play and provide encouraging signs.

Fiscal stimulus actually began before the attack. The tax rebates and adjusted withholding pushed tax-adjusted incomes up at a 12 percent pace in the third quarter.

Next, some corporate stimulus is needed. It is hoped that the stimulus package that eventually emerges from Congress -- coupled with emergency stimulus and the airline recovery and security measures -- will provide the right boost. We can't say precisely when a turnaround will come. Nor can we say when the war on terrorism will be won. But with the strongest, most technologically advanced, most resilient military in the world, we will prevail on the national security front.

What we have learned from September 11, the ultimate case study for Econ 516, is that with the strongest, most technologically advanced, most resilient economy in the world, we will prevail on the economic front.